



INNOVATIVE BUSINESS MODELS: A STUDY WITH REFERENCE TO INDIAN BANKING SECTOR

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ABSTRACT

The Indian Banking Industry has been witnessing a huge reformation in the last two decades. The commencement of financial sector reforms has led to the intensification of the Indian Banking sector and has made it more and more competitive. Banks in India are changing the way they do business. There has been a significant change in customer expectation with regard to banking services. Banks have started altering their business model by emphasising more on provision of better customer experience rather than on mere selling of products. The increasing use of technology in banking process has led to the availability of core banking solutions, internet banking credit and debit cards, mobile banking etc. This transition to the new business environment has created newer demands on the banking sector such as increased workflow and customer access to banking transactions through the electronic mode. Most banks in India are working towards providing customised products that meet the requirements of their diverse clientele

The financial products offered by banks are much more when compared to non-banking companies and therefore the need to develop customer centric products assumes paramount significance in an era of heightened competition. The banking sector in India is no exception to this growing trend of staying ahead in the race to retain customers through their innovative practices. Indian banks are aspiring high and are moving towards implementing a world class internet banking capability. The presence of a large unbanked population provides the scope for innovation in delivery. Banks in India have started leveraging the use of technology to achieve competitive advantage by reaching out to masses in a cost-effective manner. The use of technology providing services to a customer segment with differentiated needs and creating value through it has become a noticeable trend in the Indian banking system. Digital banking seems to be a preferred choice among the new generation banking customers. They are moving towards building a digital business model. The present research paper is an attempt to provide an insight into the changes witnessed in the banking business model in India.

KEY WORDS: Banking, Innovation, Cost-effective, Digitisation, Business model.

Introduction

The banking sector in India is undergoing rapid transformation in the last few years. Changes in customer behavior is posing a great challenge. As per the Reserve Bank of India (RBI), India's banking sector is sufficiently capitalised and well-regulated. The financial and economic conditions in the country are far superior to any other country in the world. Credit, market and liquidity risk studies suggest that Indian banks are generally resilient and have withstood the global downturn well. Banking today is a flourishing industry, focused on technological innovation. Internet banking has emerged as the biggest focus area in the "Digital Transformation" agenda of banks.

Indian banks have technology-intensive solutions to increase revenue, enhance customer experience, optimize cost structure and manage enterprise risk. However, there is a wide variation in the technology agendas and implementation capability across different players of the banking industry. Banks are working towards enhancing core banking value by revamping the digital agenda. They are accelerating innovation in a rapidly changing risk scenario by moving from cash to electronic modes of payment.

Indian banking industry has recently witnessed the roll out of innovative banking models like payments and small finance banks. The central bank granted in-principle approval to 11 payments banks and 10 small finance banks in FY 2015-16. RBI's new measures may go a long way in helping the restructuring of the domestic banking industry. According to the Indian Brand Equity Foundation report in February 2017, the Indian banking system consists of 26 public sector banks, 25 private sector banks, 43 foreign banks, 56 regional rural banks, 1,589 urban cooperative banks and 93,550 rural cooperative banks, in addition to cooperative credit institutions. Public-sector banks control nearly 80 percent of the market, thereby leaving comparatively much smaller shares for its private peers. Banks are also encouraging their customers to manage their finances using mobile phones. Standard & Poor's estimates that credit growth in India's banking sector would improve to 11-13 per cent in FY17 from less than 10 per cent in the second half of FY14.

Review of Literature

The banking business has undergone changes in the regulation of the sector, changes in consumers' demand for services, technological changes, and the entry of new competitors from businesses outside banking (Gardener et al., 1999). A marketing approach to banking involves strategic determination of desired customer base, identifying their current and future needs creating need satisfying benefits which differentiate the organisation from its competitors communicating and delivering these benefits to the market place (Bettinger, 1985). According to Jacoby and Chestnut (1978), firms should strive to maintain long term relationships with their customers to obtain the advantages of a clientele loyal to the firm. Bhattacharya (1989) provided a marketing approach to banking services by

identifying different segments of customers and their needs in order to provide appropriate range of services. Magretta (2002) defines business models as "stories that explain how enterprises work." Magretta's approach highlights two fundamental questions that any business model should answer, one related to the value provided to the customer and the other to the organization's ability to capture value in the process of serving customers. According to Amit and Zott (2001) "A business model depicts the content, structure, and governance of transactions designed so as to create value through the exploitation of business opportunities." Baden-Fuller, MacMillan, Demil, and Lecocq (2006) when they define *business model* as "the logic of the firm, the way it operates and how it creates value for its stakeholders."

The literature on financial services indicates that banks should focus their efforts on three fundamental points: shareholder value (Ingo, 1997), employee value (Payne et al., 1999) and consumer perceived value (Reidenbach, 1996; Kelly, 1998; Marple and Zimmerman, 1999). The quality of service is a fundamental element in the perception of perceived value, as it is the most difficult thing for competitors to imitate (Parasuraman and Grewal, 2000). Electronic banking has been around for quite some time in the form of automated teller machines (ATMs) and telephone transactions. In more recent times, it has been transformed by the internet – a new delivery channel that has facilitated banking transactions for both customers and banks (Nitsure, 2003). As a part of strategic decisions, banks in India have been investing and continued to invest enormous amount of funds on computer and related technologies expecting substantial payoff. (Surulivel and Charumathi 2013). Internet banking is predicted to transform and revolutionize traditional banking industry (Mols, 2000). Banking services are easily digitalized and automated and, thus, from an operational perspective, lend themselves to the internet (Elliot and Loebbecke 2000; Daniel, 1999) the potential competitive advantage of the internet for banks lies in the areas of cost reduction and satisfaction of consumer needs. Managing service is different from managing goods because of long-recognized differences between the nature of service and the nature of goods (Parasuraman et al. 1985). Some of the notable characteristics of service that make managing service different are (1) intangibility, (2) heterogeneity, (3) simultaneity of production and consumption, and (4) perishability.

Donald. Mullineaux (2010) established empirically that marketing in the form of advertising and promotion or adding new branches by US banks improved their performance in the areas of profits and market share. Baker Michael (2009) defined and presented a performance approach for implementing best practices in Financial Institutions. financial institutions can gain the greatest value from innovations in customer relationship management (CRM) technologies. Cornell, Halley (2003) focus on the importance online banking services offered by banks and the Competitive advantage of online banking.

Emerging Scenario in the Business Model of the Indian Banking industry :

The Indian Banking Industry is all set for spectacular growth in the coming years with total banking sector credit expected to rise at a CAGR of 2.5% to reach USD 15.9 million by 2016 according to the Indian brand equity foundation report (Dec 2016). They are focused on technology innovation as the increase in disposable incomes of the working population has raised the demand for banking and related services. Most banks in India have started improving their technology infrastructure to enhance customer experience and competitive advantage. The shift towards internet banking has been on the rise as a large segment of the population in India is young and the average age in India would be 29 years by the year 2020. Banks across India are adopting business intelligence (BI) and analytics to drive their overall profitability. Change in customer buying preferences and coping with changes in Technology will be the key factors that will drive transformation in the banking sector in the next few years.

As opportunities for building stronger relationships exist banks in India are expanding customer base by selling more products to their current customers and convincing new customers that they provide complete banking experience. A deep understanding of individual consumer financial goals, needs and inclinations will help in devising better strategies to serve them. Banks are changing their business model with the objective of developing a customer centric focus which would be very different from the product based business model that has been adopted till recently.

Bank technology is moving towards digital innovation. Banks introduce new services and technology to improve connectivity with customers, automate processes and provide seamless customer experience. Government initiatives, such as Skill India, Make in India, Digital India and others are expected to encourage banks in the use of digital technology in their services. Banks work towards providing good customer experience, reduce overall costs and stand out from the competition by integrating unique delivery channels, offering mobile solutions and learning from big data.

Digital strategist's world over opine that leaders in the financial industry identify the critical online, digital, mobile and social media trend that are redefining marketers' strategies and budgets. Banks make use of content marketing to attracting and maintaining consumers by integrating multi-channel approaches such as affiliate marketing, direct mail, display advertising, email marketing, Search Engine Optimization and Marketing (SEO/SEM), blogging etc. Banks are integrating more branded videos into their digital strategies, to make interactive content available along all online channels. Building and offering responsive websites and optimising mobile usage has become key to marketing of banking services. Banks are also looking at big data crunching as a means to identify customer credit limits.

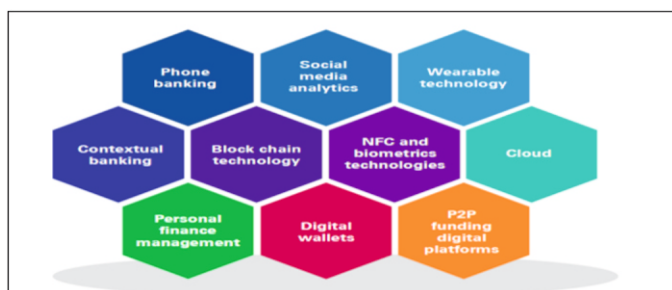


Fig :1 Major digital innovations in the Finance sector

Source: KPMG in India's Analysis based on Industry discussions 2016.

The success of banks in marketing of these digital banking services depends on the ability of the bank to make use of the technology and the willingness of its customers to adopt this technology.

Mobile banking services have become popular with the increase in the use of smart phones. private sector banks are leaders in the marketing of mobile applications when compared to public sector banks. However unwanted sales messages result in customers shifting to other providers. Most banks in India offer basic banking services, bill payment, customised offer, location based offers using mobile banking services. Banks also market their services using social media platforms as it helps in obtaining data about its customers which when subjected to data analytics can provide information about customers. This ensures delivery of better services and can help in identifying prospective loan defaulters. Most banks in India have accounts on social media platforms. For example, Kotak Mahindra bank offers a bank-agnostic payment service for Facebook. This allows its Indian account holders to make fund transfer to any person on their friends list. Similarly, State Bank of India unveiled 'SBI Mingle', as social media banking platform for Twitter & Facebook users

With a projected growth rate of 35% between 2015 and 2020 in the biometrics market in India most banks in India have started making use of scanning finger print and Aadhar number to generate Know your customer (KYC) details automatically. ICICI bank announced the launch of the country's first "contactless"

debit and credit cards, enabling its customers to make electronic payments by just waving the cards near the merchant terminal in lieu of dipping or swiping them. These cards are based on Near Field Communication (NFC) Technology which provides customers the improved convenience of speed as these cards require significantly less time than traditional cards to complete a transaction along with enhanced security as they remain in control of the customer. The use of Cloud Technology by banks in India is slow due to the regulations laid down by the RBI Cloud Security Framework for the Indian Banking Sector 2013. However, use of cloud technology in the future by the banks is expected to result in several key benefits such as reduced costs, improved flexibility, improved operational efficiency and agility (increased centralised management of data), automatic scalability, efficient client service and business continuity. Indian banks are focussing on SMAC (Social, Mobile Analytics and cloud) techniques to reach new customers.

In the area of personal financial planning, banks have found innovative ways of providing services to their customers. ICICI securities has launched "Track & Act", 'A Robo Advisory Platform' aimed at effortless tracking and investing for its customers. For every financial goal, ICICI securities will choose the best path from over 2.5 million simulations that are generated using algorithms for each customer's annual investments for these goals. The Robo advisory platform monitors deviations in the customers target asset allocation, target savings and Target portfolio and automatically prompts the action required. Banks are also offering Digital wallets. The Indian m-wallet market is anticipated to grow at 2.25% CAGR to become USD 5.12 billion by 2020. ICICI bank has launched a new e-wallet service called "Pockets" which enables customers to carry out online transactions using money funded through their bank accounts. Contextual banking is another innovative service offering seamless banking where financial offers are made at the time and place of need. Portals such as CIBIL X Press Acquire provide credit scores to prospective borrowers of bank loans thereby facilitating real time loan offers from banks. Block chain technology will be another milestone in banking services in India with the RBI providing endorsement of this in December 2015. Block chain is expected to improve back end operations in the financial sector especially in trade finance, syndicated loans, crowd funding platforms, bonds and private placement markets. This would facilitate automation in activities such as clearing settlement, transfer and trading activities. P2P funding is another promising service area enabling raising of capital by start-ups. Wearables devices are also becoming popular trends in banking services. Axis bank has tied up with GOQii to launch a wearable device for its customers. This device will allow users to make NFC payments and will also carry fitness features of GOQii. The bank is expected to incentivise customers to adopt healthier lifestyle, like offering loyalty points on walking a certain number of steps every week. ICICI Bank also has launched banking applications called "iwear" which will provide transactional and informational services for their customers. Banks are also entering into strategic partnerships with fintech firms with expertise to match customer expectations. The World retail banking report 2016 offers a snap shot of customer experience with banks and fin tech firms.

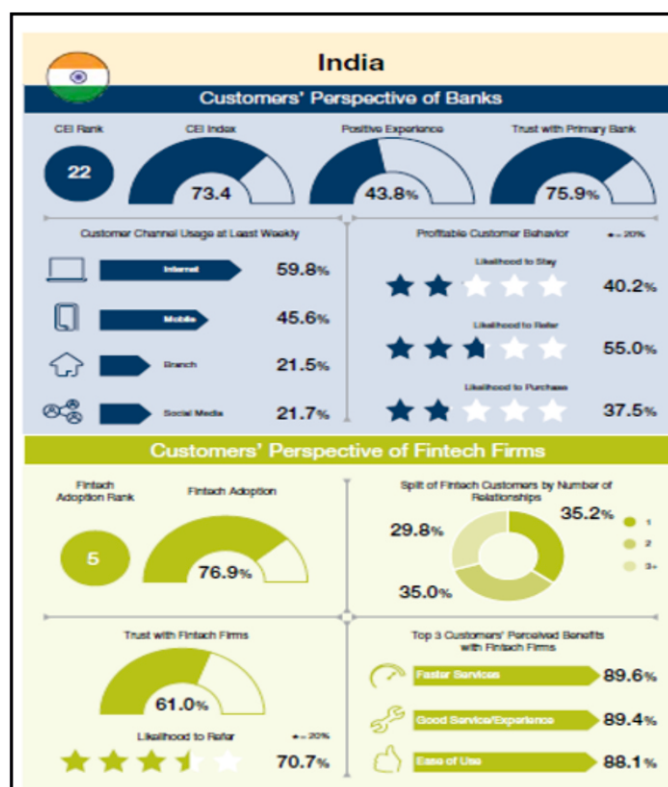


Fig 2 : Customer Perspective of Banks and Fintech firms.

Source: 2016 Retail banking Voice of the Customer Survey, Cap Gemini

As regards India customer usage channel on a weekly basis internet was at the top with 59.8%, followed by mobile with 45.6%, social media and branch accounted for 21.7% and 21.5% respectively. Customer perspective of fintech firms showed a 76.9% for fintech adoption with a trust factor of 70.7%. Customers perceived faster services, good service experience and ease of use as benefits accruing from fintech firms in India.

Banks are reinventing their business model by developing customer retention strategies and improving service quality initiatives. This has been made possible as they now concentrate on the relationship selling model by predicting customer demand in advance. Globalisation, monetary policy and regulation have caused a massive shift in business models of banks. Following the RBI mandate on core banking, banks in India started implementing core banking transformation programmes. Centralisation of customer data, streamlining of teller operations and network were established to connect branches to a common platform. They continue to transform their business by deploying technology intensive solutions.

Banks have started adopting segmentation process that serves priority customers with customised products. They now adopt a strategic pricing strategy that maximises what customers are willing to pay based on value perceptions, generating the most profit for each relationship. Achieving customer segmentation is no easy task as it will involve a strategic outlook to product development, pricing and marketing. It is important to understand factors that promote customer loyalty and attrition. They need to adopt a strategic pricing strategy that maximises what customers are willing to pay based on value perceptions, generating the most profit for each relationship. Delivering consistent and efficient experience across channels and integration across them will ensure delivery of right product offering to right customer at the right time.

According to the Boston Consulting Group (BCG) report 2016, product expertise, price and amount of capital are seen as the biggest strengths of the Indian banking sector while exception handling, service charges and technology are the weaknesses. In recent times the quality of relationship management has deteriorated. Banks are faced with huge challenge of converting technology awareness among its customers to technology usage by the. While corporate banking is still heavily reliant on relationship managers, the shift to mobile banking looks imminent. More than 40% of the corporate banking customers especially those from the logistics, retail and FMCG and Telecom and IT are willing to pay for value added services from banks. This is a green area for banking services especially the ones such as online back up and financial analytical tools. The small business sector is still dependent on cash and cheque facilities. Banks are hoping that access to internet by medium and small enterprises will increase their preference for online banking in the coming years. The lack of knowledge on how to use mobile applications and the complexity of information in online banking is a major cause for slow adoption by customers. Banks must invest in creating awareness of digital banking among all customer segments. Once the awareness gets converted to usage, customers usually get satisfaction from the online experience and this will help banks optimise their costs. The number of online customers in India is expected to grow from 60 million in 2015 to 173 million by 2020. It has been found that there is a positive correlation between the number of channels offered by the bank and the number of products used by the customers. Customers prefer digital banking services in the areas of payment, saving and expenditure and investment.

The wide scope and convenience of online banking has shifted the focus from branch banking to Net Banking. Banks have embarked on the development of innovative products and advanced risk management products to capture the market share. The launch of core banking initiatives has strengthened the static and transactional data base of banks. Banks are exploring the possibilities of partnering with fintech firms to be able to transition into the digital banking ecosystem as the penetration of Fintech firms is the highest in the emerging and younger customers. Banks and Fintech firms need to be proactive, work together and leverage each other's strengths to create the best financial ecosystem and reduce the risk of being marginalised as it evolves.

To capture the potential value of digital finance, there are three important aspects that need to be developed namely widespread digital infrastructure, dynamic and sustainable financial-services markets, and products that people prefer to existing, often informal, alternatives. Addressing all three can enable broad and rapid adoption of digital finance by the majority of individuals and businesses in emerging economies. Banks in India are moving towards a digital model by thinking differently about their digital channels. They need to provide customers information on their current and prospective financial health, and equip them to make better financial decisions.

Banks are transforming customer experience by educating customers on the ease of transacting. They have started combining the power of the web with analytics to provide useful insights on how customers can manage their finances. The integration of web channel with branch banking will facilitate availability of customised product offerings. The vast customer data base available with banks when combined with business analytics will increase the speed of technology adoption by banks. Building and implementing the digital business model will require banks to fundamentally change the banking business model in terms of

customer segments, revenue impact and the cost of providing service. Channel governance and integration with enterprise processes is the need of the hour. Besides banks also have to adopt a methodology to educate and train staff on the benefits of the internet channel.

The Road ahead for banks in India :

As digitisation encompasses all banking functions and governments drive towards a cashless economy surges ahead, there is pronounced change that is being witnessed with regard to banking business models. Technological innovation has thrown up key challenges across the entire value chain. Some of the significant developments in the technology driven business model of banking include use of digital authentication using biometric technology, payments and transaction simplification using block chain technology, availability of automated investment advisory services, automation of back office operations, providing an enjoyable customer experience with the help of gamification.

Digitisation has paved the way for the emergence of new competitors to banks in the form of financial technology firms. They pose serious challenges to banks in the areas of payments as they are able to provide seamless integration of payment processes. Besides deposits and lending functions of banks are also challenged by availability of alternative lending platforms. Investment management, market provisioning and capital raising are also areas where banks will face competition from these firms. These challenges can be dealt with by banks to a certain extent as still entry barriers for new banking companies in India is high. Most Indian banks have been able to survive with the traditional model in which customer trust is a key driver. There are some banks which are reinventing their business model with more spend on digitisation to stay ahead of the traditional banks. But the fierce competition will continue with the emergence of more financial service providers.

A Recent report on the future business models in banking by Deloitte in 2016, banks have to choose among the five business models as their value chain continues to disintegrate due to the emergence of severe competition from fintech firms. Banks can choose to be a) Trusted advisor b) Product leader c) Transaction champion d) Managed service provider e) Universal bank.

Banks which choose Trusted advisor as their business model build on customer trust and offer customised value added services as they understand their client needs well. Banks which adopt Product leader business model offer innovative products at premium prices. They are able to integrate new technology in their product offerings and are valued by their customers for the quality of their products. Those banks which adopt transaction champion model gain from the economies of scale by forging partnerships with other service providers from banking and non-banking background. Banks which choose to be managed service providers provide specific banking services to other providers. These services include regulatory insights such as KYC to investment advice. The Universal bank model will include a comprehensive product offering across industry sectors. They have a diversified business mix which meets all kinds of customer needs. The choice of the business model will depend on the evaluation by the bank of its strengths, weaknesses, opportunities and threats.

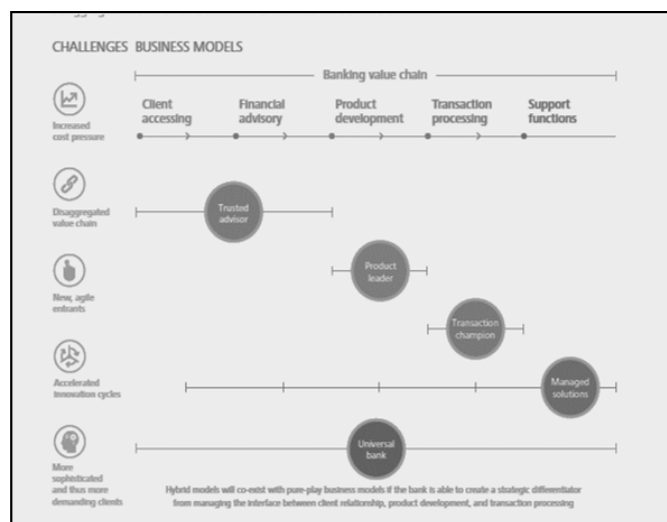


Fig: 3 Business Models in Banking

Source: 2016 Deloitte report on Banking Business models of the Future

As digitalisation continues to remain an opportunity and challenge for the Indian banking sector, in order to be successful, they will have to focus on path breaking innovation, develop flexibility to adapt and implement new ideas which will help in educating and incentivising customers to move to digital channels.

CONCLUSION:

From the past two decades, the Indian banking sector has completely trans-

formed. It launches the innovative models to makes serving customers convenient and saves a lot of time on the part of the employees who continuously searching for customer data. This improves service excellence and leads to more customer satisfaction, in the long run retention. In terms of cost to the banks, they save a lot in employing newer staff and are able to perform more efficiently with less capacity.

The government's focus on digital India has resulted in a shift towards cashless economy. The traditional banks in India have started facing competition from new banks as well as from technology focussed industries. These banks have been forced to adopt digitalisation as Non-banking finance companies, telecom companies, postal service providers, payment service providers have all been granted payment licenses. Payment banks can appoint their merchants and users would be able to pay them electronically. However, these digitalisation channels used by banks are at different stages of maturity.

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